No. 12,102

IN THE

United States Court of Appeals

For the Ninth Circuit

JOE BALESTRIERI AND COMPANY,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

REPLY BRIEF FOR PETITIONER.

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PRELIMINARY STATEMENT.

The respondent's brief in this matter was served upon counsel for the petitioner on May 5, and as the 10th day thereafter falls upon a Sunday, petitioner's time for filing its brief expires on Monday, May 16.

I.

THE RESPONDENT'S ARGUMENT THAT PETITIONER WAS A GUARANTOR OF THE PARTNERSHIP'S OBLIGATION TO PACIFIC VEGETABLE OIL CORPORATION ON THE MILLING VENTURE. (R.B. pp. 9-20.)

The respondent now tacitly concedes in the heading of his argument and in the context thereof on page 9 of his brief, what the Tax Court wholly failed to find,

despite the uncontradicted and unimpeached evidence presented to it, that is, that there was a separate milling venture distinct and apart from the partnership's mining operations. The respondent's position now is that there was such a venture, but that the petitioner corporation was not a participant therein, despite the fact that it was to have 50% of the net profits of that venture.

No fault can be found with respondent's statements of the history of the statutory provisions in California with respect to guaranty and suretyship, and the general legal propositions set forth in the early portion of his argument on pages 10 to 12 of his brief. However it is impossible to understand how the respondent reaches the conclusion that he does, reasoning from the law as applied to the documents and other evidence involved in this case.

Thus after admitting that the word "guaranty" is ambiguous and may mean many different things, he states without any authority whatsoever (Br. p. 12) "It is clear, however, that the use of the word 'guaranty' or 'guarantee' is entitled to great weight as evidence of what the parties intended".

The respondent further admits that interpretation of the agreement is difficult because made by laymen without regard for legal refinements. The testimony of W. E. Otto on the matter, however, is clear and explicit:

> "I explained to Pacific Vegetable Oil the proposition. He said, 'Reduce it to writing and I will consider it.'

I did submit it to him, myself, on behalf of the partnership, and his reply after that was that he would go along with the deal, provided that we'd have the meeting of the Board of Directors of the fish corporation agree to underwrite, or absorb, any loss that might occur. We never thought there could possibly be any loss, we thought it was a bonanza in our lap rather than possible loss." (Tr. 25.)

And again:

"We offered Joe Balestrieri, the partnership offered Joe Balestrieri and Company one-half participation in the earnings of that venture, which we thought was very liberal, and in exchange for that they were to *guarantee us* for any losses that might occur on the venture." (Emphasis supplied.)

"Q. What do you mean by the word 'guarantee'?"

"A. Well, if we ran into difficulties and ran into a loss, they would absorb any loss that might occur.

Q. In other words, the agreements of the petitioner corporation related only to the milling venture?"

A. That was the reimbursement, that's right." (Tr. 27.)

* * * * * * *

"* * * They accepted the proposal, and in consideration of the 50 per cent participation that they would have in the profit, that they would absorb any losses that might occur." (Tr. 28.)

Both of the witnesses showed more than a customary ignorance of technical legal meanings of words

used by them in their testimony. It is obvious from their grammar that neither has had the advantage of extensive education, although the broken English used by Mr. Balestrieri in his testimony is not fully reflected in the transcript.

The testimony of the witnesses is confirmed by the agreement itself and by the circumstances surrounding it in the following particulars:

1. The agreement was not made with the creditor but with the party seeking credit.

2. The venture was regarded as a bonanza, and yet 50% of the net profits was to be given the petitioner corporation.

3. The language used in the agreement supports the testimony. The letter to petitioner (Tr. 75) is headed:

> "Offer to *participate* in profits of Chrome Milling Operation to be handled by this partnership in consideration of guaranteeing *venture.*"

And the letter concludes (Tr. 76):

> "In the event you decide to *participate in this venture,* please have your Board of Directors ratify same and formally confirm same to us in writing."

Similarly, in the minutes of the petitioner corporation, the following language appears (Tr. 77):

> "* * * the proposal to participate in one-fourth (sic) of the earnings of the Chrome Milling venture at Castella was accepted. The corporation in turn guaranteed any losses or deficits that may occur on money borrowed from the Pacific

> Vegetable Oil Corporation on the crome (sic) milling venture. * * *"

And the final document involved (Tr. 78) refers to "our participation in your Chrome Milling Venture," and further states:

> "* * * We herewith accept this proposal of yours to participate in the profits of your chrome milling operation and we in turn guarantee any losses should they occur."

On the first point above noted, the respondent pays no attention to the fact that a contract of guaranty must be between the guarantor and the creditor, and at least normally requires a delivery to and acceptance by the creditor.

> 24 *Am. Jur.* 899-900.

The agreement herein made was not with the creditor and is not couched in the ordinary terms of a contract of guaranty. The loss which petitioner "guaranteed" was not limited to the loss which Pacific Vegetable Oil might otherwise incur—because of the principal's inability to pay—but the entire loss on the milling venture (which was to be entirely financed by Pacific Vegetable Oil). Under the language of the agreement, if the partnership made a profit on its mining venture that profit could not be used to off-set any loss sustained on the milling venture, thereby reducing petitioner's obligations, but such loss was to be petitioner's entirely and exclusively.

The respondent wholly misses the point of the cases and other authorities cited by petitioner on pages 12

to 15 of petitioner's opening brief. These cases establish that the contract containing the promise from petitioner to the partnership, would, even if entirely oral, be outside the statute of frauds and make petitioner liable as principal, to the partnership and, incidentally, to Pacific Vegetable Oil Corporation. Being liable as principal, it was not a guarantor.

As against this point the respondent's only argument is the circuitous one that because the ambiguous word "guaranty" was used in the agreement, what was meant was a strictly legal guaranty, and the further proposition that Pacific Vegetable Oil would not have financed the venture had petitioner's credit not been available to it. As noted in petitioner's opening brief, however, Pacific Vegetable Oil had greater protection with the petitioner as a principal obligor than as a guarantor.

The limitation of the agreement to one of guaranty for the benefit of Pacific Vegetable Oil is inconsistent with the basic circumstances. The parties fully anticipated to make very large profits from the venture. The petitioner was to have 50% of those profits and Pacific Vegetable Oil was to have 25% for a limited period. Thus the petitioner corporation had a far greater interest in the profits of the venture than did the three members of the partnership. Respondent contends that each one of the three who had an 8⅓% interest in the profits comprised the sole joint venturers and would eliminate the entity which had 50%. An agreement to absorb all of the losses of the venture is very much more in accord with a 50% interest in

the profits than is an agreement of guaranty to a third person.

Respondent's argument on pages 13 to 16 is exceedingly circuitous, and essentially assumes that a true guaranty was intended and made. The respondent makes no answer to the petitioner's authorities establishing that the agreement in question had been made with the partnership rather than with Pacific Vegetable Oil.

It should perhaps be emphasized that petitioner at all times treated the transaction as an agreement to absorb the losses on the milling venture. It reported the loss on its tax return, and recognized the direct obligation to Pacific Vegetable Oil Corporation, making payments thereon, principally in years subsequent to the taxable year here involvel. No effort at any time was made by either the petitioner or Pacific Vegetable Oil Corporation to collect from the other participants.

Commencing on page 16 the respondent argues that there was no joint venture between the petitioner corporation and the partnership with respect to the milling operations. However, it is well established that the essence of a joint venture is the agreement of the parties with respect to a particular undertaking specifying the manner in which the profits and losses as between themselves shall be borne, and a presumption arises from the sharing of profits that a joint venture is made. The petitioner has throughout its proceeding referred to the agreement as one creating a joint venture, because of the limited nature of the

undertaking and the limited operations period contemplated; in some respects, because a continuity of transactions was contemplated it is possible that the term "partnership" is more clearly applicable. The difference is purely one of degree.

As stated in petitioner's brief (p. 19) the petitioner's contribution was in the nature of a capital contribution and as under the offer of Pacific Vegetable Oil, it was to entirely finance the venture; petitioner's agreement to absorb any losses that might occur, in substance made the petitioner the borrower from Pacific Vegetable Oil and its contribution in substance the entire capital of the venture.

The respondent makes a great deal of the fact that petitioner independently of its two officer shareholders had no control over the venture. This contention is utterly ridiculous, because the two officer shareholders were in control of the partnership as well as in complete control of petitioner. It is true, as stated on page 17 of respondent's brief that the authorization granted to the partnership was only with respect to this venture, and petitioner's officers were not at any time authorized by the petitioner to enter into any other ventures. If the ownership of petitioner were to be changed, the petitioner would remain sufficiently in control and management to terminate the joint venture.

The remainder of the respondent's argument on this point assumes the respondent's conclusion that the petitioner was not a participant in the venture but

was a mere guarantor to Pacific Vegetable Oil Corporation.

II.

THE RESPONDENT'S ARGUMENT THAT EVEN ASSUMING THAT THE TAXPAYER WAS A MEMBER OF A JOINT VENTURE IT IS NOT SHOWN TO BE ENTITLED TO DEDUCT A LOSS UNDER SECTION 182 OF THE CODE.

The respondent's argument under this heading is somewhat confusing because it entirely ignores the agreement between the parties, a portion of which consists of the letter addressed to Pacific Vegetable Oil Corporation. Under that agreement Pacific Vegetable Oil Corporation was to entirely and exclusively finance the operation of the joint venture, in the purchase, transportation, milling and sale of chrome ore. There is no question but what any loss sustained in this activity would be an ordinary operating loss of the venture and no issue was raised with respect thereto in the deficiency notice or otherwise.

Similarly, the loss which petitioner agreed to assume was solely in connection with the financing of the milling venture by Pacific Vegetable Oil Corporation. If any greater loss existed it was not that of the petitioner and the only way a greater loss could have been sustained was if the individuals interested in the partnership, or the partnership itself, supplied additional capital. The respondent now assumes wholly without evidence, and contrary to the testimony of Mr. Otto (Tr. 30, 42-43) and of Mr. Balestrieri (Tr. 47), that

the amount of the loss was not established. In this testimony the amount of the loss of $22,229.37 was not only established, but the way in which the loss arose was also confirmed as being in accordance with the agreement.

III.

THE RESPONDENT'S ARGUMENT THAT THE TAX COURT DID NOT ABUSE ITS DISCRETION IN DENYING THE REQUEST OF TAXPAYER'S COUNSEL FOR ADDITIONAL TIME TO PREPARE HIS CASE.

The respondent's argument on this issue is deserving of very little recognition, particularly in view of the statements made in other portions of his brief as to the inadequacy of the evidence on the pertinent issues. On page 22 of the brief, respondent makes a point of the facts that the hearing did not commence until 5:30 p.m., but does not point out that the petitioner's counsel was required to be in Court and ready to proceed at any minute during the course of the day in question, and consequently did not have that day available to examine books and records and interview witnesses.

Petitioner's counsel is aware of the numerous instances in which the testimony adduced could have been fortified and strengthened in this proceeding and believes very strongly that had a little greater preparatory time been alloted the Tax Court would never have found (what respondent now concedes to be erroneously found) that the testimony of petitioner's

witnesses was inconsistent with the known facts. Sketchy though the evidence is in certain particulars, petitioner nevertheless believes that it is adequate and establishes petitioner's right to the deduction claimed.

CONCLUSION.

The Tax Court's decision being contrary to established legal principles, and to the evidence adduced, is clearly erroneous and should be reversed.

Dated, San Francisco, California,
May 16, 1949.

Respectfully submitted,
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